UNITED
NATIONS

E

Economic and Social Council

Distr.
GENERAL

E/C.10/AC.3/1994/6
13 January 1994

ORIGINAL: ENGLISH

COMMISSION ON TRANSNATIONAL CORPORATIONS
Intergovernmental Working Group of
Experts on International Standards
of Accounting and Reporting
Twelfth session
Geneva, 7-15 March 1994
Item 7 of the provisional agenda*

ACCOUNTING FOR GOVERNMENT GRANTS AND CONCESSIONS

Report of the UNCTAD secretariat

SUMMARY

Government grants and concessions can have a significant financial impact upon the operations of enterprises, whether State owned or influenced or entirely privately owned. Governments use grants and concessions to implement fiscal and monetary policies and often to meet social objectives. The International Accounting Standards Committee's International Accounting Standard (IAS) 20 prescribes the accounting treatment and related disclosures of government assistance. National conformity with IAS 20 is increasing; however, some countries have recently developed national procedures which are not in harmony with the IAS 20, yet previous national practice did comply. Some countries offer very little governmental assistance and consequently accounting standards dealing with this issue are not highly developed. One of the contentious aspects of this topic is whether the assistance represents a capital item or more in the nature of revenue.

* E/C.10/AC.3/1994/1.

CONTENTS

	Paragraphs	Page
INTRODUCTION	1 - 5	3
I. SUMMARY OF FINDINGS	6 - 11	3
II. ACCOUNTING TREATMENT FOR GOVERNMENT GRANTS AND CONCESSIONS	12 - 48	5
A. Government grants and concessions from the Government's perspective	12 - 17	5
B. Government grants and concessions from the recipient's perspective	18 - 41	6
C. Global accounting practices and consistency in the treatment of government grants and concessions	42 - 48	11
III. ECONOMIC IMPACT AND EXTENT OF GRANTS	49 - 50	15
IV. CONCLUSIONS AND RECOMMENDATIONS	51 - 53	15

INTRODUCTION

1. This report was prepared in order to provide the Intergovernmental Working Group of Experts on International Standards of Accounting and Reporting with a review of the issues and practices surrounding the accounting for government grants and concessions.

2. The most controversial aspect of this topic is whether the receipt of a grant represents income or is of a capital nature. There is general consensus that the item should not be recognized until receipt is absolutely certain and the enterprise has fulfilled all of the conditions attached to the assistance.

3. Firstly, this report defines the terms "government grant", "concessions" and "assistance"; then it examines the issues involved. Government assistance can cover a very wide range of activities: from a straightforward and easy to measure cash transfer, to more subtle and difficult to quantify forms such as free marketing advice, import protection in the form of duties and tariffs, or policies such as government purchasing contracts which favour domestic goods and services. To quantify the extent and impact of some of these latter forms of intangible government assistance would simply represent educated guesswork.

4. The International Accounting Standards Committee (IASC) has issued International Accounting Standard (IAS) 20, "Accounting for Government Grants and Disclosure of Government Assistance", and most national standards that deal with this matter are generally in conformity with IAS 20.

5. This report is presented in four parts: first there is a summary of findings; secondly, a discussion of the issues surrounding the accounting treatment; thirdly, a brief description of the extent of government grants in some countries; and, lastly, conclusions and recommendations.

I. SUMMARY OF FINDINGS

6. The significance of government grants and concessions cannot be overlooked in both the developed and developing economies where Governments are involved to a great extent in the affairs of public and private enterprises. What is most peculiar about these types of transactions is that generally the transferring Government does not receive any goods or services or receive a return on its investment. A direct "exchange relationship" is often not present, which is most unique and separates this type of transaction from commercial transactions.

7. This paper does not cover the following:

(a) Entitlements, which are considered to be transfers made by the Government to individuals or corporations which meet certain criteria: for instance unemployment benefits, family allowances and other forms of social welfare. These benefits are non-discretionary, meaning that government legislation specifies who is eligible for the transfer in addition to stating the amount;

(b) Government loans which are made on a commercial basis are also not considered, because they would normally be treated in an identical manner to an arms-length commercial transaction;

(c) Indirect government assistance, such as: a policy to procure from domestic producers and manufacturers, which can often direct substantial amounts of economic activity towards an enterprise; or the provision of government guarantees or underwritings. It is very difficult to determine the precise benefit to an enterprise from this preferential treatment. Although sales or income from the Government can be readily identified and quantified, the issue is really the benefit of the "favouritism" bestowed upon the enterprise. The Government under normal operating procedures may well have intended to procure from the enterprise in question, so there has been no government assistance as the transaction represents "business as usual".

8. Other forms of indirect government assistance may include import protection in the form of duties and tariffs, or more subtle protection such as local regulations and licensing laws. It may be possible to calculate an estimate of the amount of assistance received if the rate of import duty is applied to the selling price of goods, although it would be a very approximate calculation and it is incorrect to assume that import duties affect the selling price in such a direct manner. Rules and regulations which inhibit or restrict foreign goods from entering the domestic market offer protection against competition and are therefore a form of assistance. However, it would be very difficult to measure in monetary terms the magnitude of this assistance. Additionally, Governments often provide free advice or consultancy services, or promote goods for foreign trade, which all bestows benefits upon enterprises. To the extent that such forms of assistance have a material impact upon an enterprise's financial statements, the nature of the assistance should be disclosed and thoroughly explained.

9. The following forms of government grants and assistance are within the scope of this paper and are defined as follows:

(a) Government assistance is government action designed to convey an economic benefit to a particular enterprise or range of enterprises which qualify under certain criteria;

(b) Government concessions are incentives to encourage an enterprise to undertake some activity to which it might not otherwise have agreed;

(c) Grants are government assistance in the form of resource transfers to an enterprise in return for compliance with certain conditions specified within the agreement or offer.

10. Grants may relate to assets whereby an enterprise must purchase or construct fixed assets, or to the performance of certain services such as research and development, either theoretical or applied. Various terms and conditions are often associated with such grants. Alternatively, grants may relate to income, such as compensation for loss of income due to a particular government policy: for example, compensation for loss of income due to

restrictions on the use of forest areas for logging purposes, or for restricting agricultural production.

11. Some transfers may be combinations of several types of assistance; hence it is essential to consider all characteristics of the transfer to determine the most appropriate treatment.

II. ACCOUNTING TREATMENT FOR GOVERNMENT GRANTS AND CONCESSIONS

A. Government grants and concessions from the Government's perspective

Government loans

12. Financial institutions lend money to earn a return. Governments may do likewise, but Governments also lend funds at minimal interests rates, often in the role of a "lender of last resort", or to implement a policy objective.

13. Due to the differing nature of these loans, traditional accounting treatments may not truly present the most accurate presentation of transactions. For example, for the 1989/90 fiscal year, Canadian government loans at the national, provincial and territorial levels resulted in loans receivable in excess of Can$ 41 billion. 1/ These loans consisted of amounts to be repaid through future government assistance and concessionary loans. Clearly, the Canadian government is heavily involved in lending to other statutory bodies, governmental bodies and the private sector. Accurate accounting techniques must be developed and used to record concessionary loans.

Concessionary loans

14. Concessionary loans are usually issued to meet policy objectives and are often granted on terms other than commercial rates. Consider the differing value of a US$ 20 million loan on market terms over a period of 20 years, and a loan for the same period with an interest rate of 2 per cent with repayments scheduled to commence after 10 years. The loans have the same face value when they are originally issued; however, clearly, the value to the government and to the recipient is significantly different.

15. The traditional historical cost accounting model does not accurately present the transaction. Net present value techniques offer a more accurate valuation. If the full value of the loan was recorded, the loan would be repaid over time and the lower rate of return on the interest income would be recognized. However, the opportunity cost of the concession is not reflected in the financial statements and it should be disclosed by notation.

16. An alternative treatment is to recognize the full cost of the concession when the loan is granted so that the cost of the decision to make the concession is not passed to future government administrations. Also, by booking the loan at the lower value, the government immediately recognizes that it has accepted an asset at a value less than the cash disbursed. Significant concessionary

loans could be considered as having two components: the grant component which represents the cost of the concession, and the loan component. Present value techniques could be used to quantify the grant and loan components. 2/

Loans to be repaid through future appropriations

17. A Government may provide assistance to an enterprise to enable repayment of a loan from a third party or previously granted by the Government itself. Such a loan cannot really be considered an asset by the Government, because in a sense the government is really repaying itself by making such assistance available to the debtor. It may appear logical to write the loan off. However, this would not address the underlying substance of the transaction and the Government's funding relationship with the borrower.

B. Government grants and concessions from the recipient's perspective

Recognition of government grants

18. To determine whether a grant should be recognized upon the receipt of government funds, the Canadian Institute of Chartered Accountants developed the following four tests:

(1) Have the events giving rise to the transfer occurred?

(2) Is the transfer authorized?

(3) Has the recipient met the eligibility criteria, if any?

(4) Can a reasonable estimate of the amount be made?

19. If there is a positive response to all of the above questions, then an economic transfer should be recognized.

20. Grants may be given to reimburse expenditures for items such as: (a) research and development costs; (b) wages, training costs, and other employment related matters; (c) transportation and relocation costs; (d) cost of utilities; and (e) capital costs for items such as land and buildings, plant and equipment, or the cost to develop natural resources.

The income approach versus the capital approach

21. This is the most controversial aspect of accounting for government grants and concessions. Once the grant is recognized, there are two methods to account for it:

(a) The capital approach whereby the receivable is credited directly to the balance sheet and is not ever amortized to the profit and loss statement; or,

(b) The income approach whereby the benefit is periodically included in the profit and loss statement.

Capital approach

22. Arguments in favour of this approach include:

(a) Government grants are intended as a financing device and should be handled as such in the balance sheet rather than be recognized as some form of income. As repayment is not usually anticipated, the most appropriate treatment is to credit the sum directly to shareholders' capital and reserves;

(b) As Government grants are not earned but represent an incentive provided by the government, it is inappropriate to consider grants as income. The government's policies could change and considerably affect the availability of grants to generate future income. This is not a factor which should be attributed to any measure of how profitably or efficiently the enterprise is being managed;

(c) Grants should be considered as an extra source of capital in addition to that supplied by shareholders. Consequently this capital should be maintained unchanged as it would be highly questionable to pay dividends from this extra source of capital which has been given, often free, to the enterprise.

Income approach

23. Justification for the income approach is as follows:

(a) Government grants confer benefits on the enterprise and its owners, and these benefits should be reflected as income over some period of time;

(b) Government grants are often intended to reimburse costs incurred, particularly for activities which may be uneconomical to perform and which would not otherwise have occurred had the grant not been received. Consequently the grant should be reflected in the income statement by matching it with the costs imposed by the requirements of the grant. The "matching principle" is paramount in supporting this argument;

(c) A grant is a receipt from a source other than shareholders, and hence should not be credited directly to the capital and reserves of the enterprise but should be recognized in the profit or loss accounts of future years;

(d) As income taxes are charged to the profit and loss account, it follows that government grants, which are also a form of government fiscal policy, should also appear in the income statement. Furthermore, some grants are subject to income tax implying that the income method is more appropriate. This treatment enables the grant to be matched with its implicit taxation implication. However, it must be noted that the taxation treatment is not a decisive factor in the determination of the most appropriate accounting treatment.

Timing and recognition of government subsidies

24. The general consensus is that the income approach is the most appropriate method of accounting for government grants and concessions. Once this approach has been elected, the enterprise must determine the most systematic and rational basis by which to allocate the income. Usually, costs directly attributable to the grant are identified and the grant is amortized as income accordingly.

Balance sheet treatment

25. If the income approach is adopted, then a grant for a capital expenditure may be recorded as deferred income and subsequently amortized in correlation with the depreciation of the associated asset, which is known as the gross method. Alternatively, the receipt could be offset against the historical cost of the asset and thus reduce periodic depreciation and amortization charges, which is the net method. Arguments against the net method include:

(a) The actual receipt of the grant never really appears within the body of the financial statements so that the transaction must be disclosed within the notes, which can be misleading. Furthermore, there is a distortionary impact upon the cash flow statement. Financial theory establishes clear distinctions between sources and applications of funds which is circumvented under the net method;

(b) Assets are usually valued at the cost price plus the expenses associated with acquisition and installation. To deduct the grant would contradict this principle;

(c) The net method distorts return on investment calculations.

26. Arguments in favour of the net treatment are:

(a) Other enterprises have access to the same grants; hence the market value of the asset under consideration decreases because all prospective purchasers can acquire the item for a lower net expenditure.

(b) Investment decisions are made on a net-of-grant basis; hence the net value represents the financial sacrifice and value that the enterprise places on the asset.

27. In principle, it is possible to adopt either treatment; however, many regulators of enterprises disallow crediting the grant directly to the fixed asset account. Many national standards, the IASC's international accounting standard, and previous ISAR recommendations allow either approach to be taken. However, the potential for confusing users of financial statements is significant when alternative accounting treatments are permitted.

Balance sheet presentation

28. If the gross method is adopted, the deferred grant should be presented on the liability side of the balance sheet. The position of the deferred grant benefit would either be (a) under shareholders' capital and reserves (with a

separate heading); (b) under the creditors or liabilities caption; or (c) as a separate heading between creditors or liabilities and shareholders' capital and reserves.

29. There is no clear resolution of the most appropriate location within the balance sheet. The same arguments used earlier in this paper assert that the shareholders' capital and reserves is an inappropriate location to report this item. Furthermore, as the grant is amortized, its income effect flows through to the capital and reserves section via the profit and loss account. On the other hand, as the deferred grant flows to capital and reserves, it should not be treated as a liability. 3/

Profit and loss statement presentation

30. It is possible to report the grant using one of two methods: either separately as income; or to directly offset the income amount against the corresponding expenditures. The first treatment is more common as it is generally considered inappropriate to net income and expense items. Furthermore, netting the grant and the expense does not facilitate comparison of the costs with other expenses not affected by a grant, or comparison with historical data when the grant may not have been previously available. Arguments in favour of the second treatment suggest that the expense may well not have been incurred had the grant not been available, hence netting is more in line with the nature of the transaction.

Non-monetary government grants

31. If an enterprise receives a non-monetary transfer such as land or other resources, it is usual practice to determine or estimate the fair value of the asset and to account for the grant and asset at that fair value. As discussed above, assistance in non-tangible forms such as international trade representation or technical advice are difficult to value and should only be disclosed in the notes to the financial statements if the assistance has a significant, tangible and quantifiable influence.

Investment tax credits

32. The Canadian Institute of Chartered Accountants has devised two approaches concerning the timing of recognition of investment tax credits: the cost reduction approach and the flow through approach. The cost reduction approach requires the investment tax credit to be accounted for in a similar manner to a government grant whereby the grant would be treated as a deferred income item and amortized as appropriate. That is, investment tax credits should be recognized as income on the same basis as the associated expenditures are charged to the profit and loss account. Alternatively, the flow through approach specifies that investment tax credits should be accounted for as a reduction of income tax expense.

33. Arguments in favour of the cost reduction approach suggest that investment tax credits are in substance government grants in the sense that they promote a particular course of action desired by the government and thereby reduce the cost of the expenditure. The anticipated tax credit is taken into account when

the decision to invest is taken. Alternatively it could be argued that the flow through approach is the most appropriate because the benefit to the enterprise is through the tax system by way of a reduction of its tax liability. The availability of the tax credit may not always be the conclusive factor in the investment decision. 4/

Concessionary loans at nil or low interest rates from the recipient's perspective

34. The benefit is not quantified, normally, by the imputation of interest, although as illustrated above, the terms and conditions of such loans can have a significant effect upon the perceived value of the loan to the enterprise. The notes to the accounts should explain the benefit derived from such loans.

Repayment of government assistance

35. An enterprise should regularly review the status of conditional government grants which it has received and ensure that the conditions continue to be met. If a breach of the conditions occurs, or appears possible, and that it is likely that some portion of the grant will need to be repaid, provision should be made for this liability. It would be the usual practice to record the item in the current year of reporting and not as a prior period adjustment because the conditions under which repayment occurs would be within the parameters of a new situation or economic condition, or some circumstance which was not prevailing or foreseen when the benefit was originally treated as income.

36. If the gross method has been utilized, the sum repayable should be deducted from the deferred income balance. If the amount of the repayment is greater than the deferred income, the excess should be charged directly to the profit and loss account.

37. If the net method is utilized, the book value of the asset should be increased by the amount repayable. Accumulated depreciation should be adjusted to account for the depreciation not charged due to the existence of the grant and the previous lower book value.

Government grants and their taxation implications

38. The terms of the grant and the particular taxation laws determine the appropriate treatment. Some government grants may be completely exempt from income tax while other grants may be assessed in the same manner as ordinary income. The fact that a grant may be tax assessed as income does not indicate that the receipt should be automatically credited to the profit and loss account. Taxation treatment should not dictate accounting treatment, and to do so could jeopardize the accounting principle that the government grant should be matched with the expenditure towards which the grant was intended to contribute.

The matching of grants and the corresponding expenditures

39. Often a grant is made for a particular activity which is easily identified and costed. However, if the grant is for general assistance with a project (such as government funds to promote the utilization of domestically produced

goods and services within a construction project) or to "encourage job creation", or some other non-financial objective, the accurate matching of the costs involved with the grant is difficult.

40. Some grants may be for a general purpose and not for a specific task or period of time, for example, a once-off grant made to an enterprise in the form of financial support. The most appropriate measure would be to record the total sum as unusual income, with adequate disclosure to ensure that the impact is clearly understood.

Disclosure requirements

41. The following information should be disclosed in the financial statements and related footnotes:

(a) The accounting policy adopted for government grants;

(b) The impact of government grants on the operating results for the period and the financial position of the enterprise (quantified, if possible);

(c) If the results of the period are significantly affected by the receipt of government assistance, the nature of the assistance, whether it will be ongoing, and the likely result if that assistance is no longer available;

(d) Unfulfilled conditions and other contingencies pertaining to government assistance;

(e) Indirect, intangible government assistance from which the enterprise has received significant benefit.

C. Global accounting practices and consistency in the treatment of government grants and concessions

42. The Working Group has previously provided recommendations on accounting and disclosure for government grants and concessions (see Conclusions on Accounting and Reporting by Transnational Corporations, paras. 171 and 172, which are also quoted in the conclusions and recommendations section of this report). IASC's International Accounting Standard 20 also deals with this topic. Briefly, this standard states that the grant should not be recognized until there is reasonable assurance that the enterprise will comply with all the conditions attaching to the grant and that the grant will be received. A grant should be recognized in the income statement over the periods necessary to match it with the related costs which it is intended to compensate. The allocation should be on a systematic basis. Grants related to assets should be presented in the balance sheet either by setting up the grant as deferred income or by deducting the amount of the grant from the related asset cost, thereby determining the net carrying amount of the asset.

43. A recent survey was conducted by the IASC regarding the use and application of international accounting standards. The outcome is presented in the following table:

Comparative national conformity to IAS 20

Country or territory	IAS adopted as a national requirement	IAS used as the basis for a national requirement	National requirement developed separately and conforms in all material respects with IAS	No national requirements but national practice generally conforms with IAS	National requirement developed separately but does not conform with IAS	No national requirements and national practice does not generally conform with IAS
Australia					X	
Austria				X		
Bahamas	X					
Barbados	X					
Belgium			X			
Botswana	X					
Brazil						X
Bulgaria		X				
Canada			X			
Colombia						X
Cyprus	X					
Czech Republic					X	
Denmark				X		
Egypt			X			
Fiji		X				
Finland					X	
France				X		
Germany			X			
Ghana						X
Greece					X	
Hong Kong						X
Hungary	a/					
Iceland			X			
India			X			
Israel			X			
Italy						X
Jamaica				X		
Japan			X			
Jordan	X					
Kenya	a/					

Country or territory	IAS adopted as a national requirement	IAS used as the basis for a national requirement	National requirement developed separately and conforms in all material respects with IAS	No national requirements but national practice generally conforms with IAS	National requirement developed separately but does not conform with IAS	No national requirements and national practice does not generally conform with IAS
Korea, Republic of					X	
Malawi	X					
Malaysia				X		
Malta				X		
Mauritius	a/					
Mexico				X		
Netherlands			X			
New Zealand			X			
Nigeria				X		
Norway			X			
Pakistan	X					
Philippines	a/					
Poland			X			
Portugal			X			
Saudi Arabia				X		
Singapore		X				
South Africa				X		
Sri Lanka		X				
Swaziland		X				
Sweden			X			
Switzerland	a/					
Taiwan, Province of China	a/					
Thailand			X			
Trinidad and Tobago				X		
United Arab Emirates				X		
United Kingdom			X			

Country or territory	IAS adopted as a national requirement	IAS used as the basis for a national requirement	National requirement developed separately and conforms in all material respects with IAS	No national requirements but national practice generally conforms with IAS	National requirement developed separately but does not conform with IAS	No national requirements and national practice does not generally conform with IAS
United States			X			
Uruguay	a/					
Zimbabwe	X					
TOTAL	8	5	17	12	5	5

Source: International Accounting Standards Committee "Survey of the use and application of International Accounting Standards 1993" draft release.

a/ Data is not available.

44. IAS 20 has either been adopted as the national requirement, used as the basis of the national requirement, or is materially consistent with national practices in the following countries: Barbados, Bulgaria, Egypt, Germany, Iceland, India, Japan, Jordan, Malawi, Norway, Poland, Thailand and United States. Relatively few countries have practices which do not conform with IAS 20. These countries include Australia, Brazil, the Czech Republic, Ghana, Greece, Italy and the Republic of Korea.

45. Of the 49 responses to the IASC questionnaire, 84 per cent of those countries had national practices or requirements which at least generally conform with IAS 20. Clearly, global accountancy treatment is reasonably well harmonized concerning this subject.

46. A survey similar to the one mentioned above was previously conducted by the IASC in 1988. As a comparison between the two surveys, it was found that there is a general trend towards increased conformity to IAS 20. India, Malta, Sri Lanka and Swaziland reported that there were no national guidelines in 1988 and that the national convention was not in harmony with the international standard. All these countries now report national standards based upon, or in compliance with, all substantial aspects of IAS 20. By contrast Greece has developed national requirements which do not conform with IAS 20. Ghana and Italy previously reported national practices or requirements which conformed with IAS 20; however this is no longer the situation.

47. Some countries have not developed national standards in this area of accounting simply because the government either does not provide grants or subsidies or the amounts concerned are minimal. Singapore and Switzerland are examples of such countries. In this situation, if group accounts are prepared for enterprises which have foreign affiliates that receive government assistance from the host country, the domestic parent company should adopt international accounting standards.

48. The European Community Accounting Directives do not contain specific provisions dealing with this topic; however general principles are identified for guidance purposes.

III. ECONOMIC IMPACT AND EXTENT OF GRANTS

49. The economic impact of government grants and concessions can be quite significant. For instance, the Canadian Institute of Chartered Accountants Public Sector Accounting and Auditing Committee found that government transfers account for 40 per cent to 60 per cent of government expenditures and revenues at all levels. In 1990 the national Government reported transfer payments of Can$ 59 billion out of total government expenditures of Can$ 143 billion. 5/ This figure does not include items of expenditure such as welfare, shared-cost agreements and research grants, in addition to grants to the private sector. Clearly the government's transfers represent a significant level of its intervention in the economy. The German government provides financial support to enterprises which aggregate between 8 per cent and 12 per cent of the purchase price or production costs of investments in new plant and equipment, provided that the item will be used within the enterprise for a period of at least three years.

50. Additionally, grants are available from a number of intergovernmental bodies and international organizations such as the European Community and the World Bank.

IV. CONCLUSIONS AND RECOMMENDATIONS

51. Uniform standards covering the accounting for government grants and concessions exist in many national accounting standards, particularly concerning the criteria for recognizing grants. However, divergence occurs in the balance sheet treatment. Although the methods prescribed are clearly defined and consistent, international and many national standards allow two alternative accounting methods. One is the gross method, and the other is the net. Two allowable standards can lead to considerable confusion and inconsistencies, especially considering that many transnational corporations and economic entities are likely to adopt procedures differing from other organizations, thereby limiting the comparability between differing financial statements.

52. In 1988 the Working Group issued a report titled Conclusions on Accounting and Reporting by Transnational Corporations. 6/ The recommendations concerning government grants and concessions fell under the heading "Subsidies granted by governments", which read as follows:

> "Information concerning government grants and assistance to business enterprises should be disclosed and include the following:
>
> "(a) The accounting policy adopted for government grants, including the methods of presentation adopted in the financial statements;

"(b) The nature and extent of government grants recognized in the financial statements and an indication of other forms of government assistance from which the enterprise has directly benefited;

"(c) Unfilled conditions and other contingencies attaching to government assistance that has been recognized;

"(d) Identification of significant project(s) or parts of a project for which government grant(s) has been given;

"(e) Any other information material enough to be disclosed.

"Reference is made to the following accounting treatment:

"(a) Government grants, including non-monetary grants at fair value, should not be recognized until there is reasonable assurance that the enterprise will comply with the conditions attaching to them, and that the grants will be received. They should not be credited directly to shareholders' interests;

"(b) Government grants should be recognized in the income statement over the periods necessary to match them with the related costs which they are intended to compensate, on a systematic basis;

"(c) Government grants related to assets, including non-monetary grants at fair value, should be presented in the balance sheet either by setting up the grant as deferred income or deducting the grants in arriving at the carrying amount of the asset;

"(d) A government grant that becomes receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to the enterprise with no further related costs should be recognized in the income statement of the period in which it becomes receivable, as an unusual item if appropriate;

"(e) A government grant that becomes repayable should be accounted for as a revision to an accounting estimate. Repayment of a grant related to income should be applied first against any unamortized deferred credit set up in respect of the grant. To the extent that the repayment exceeds any such deferred credit, or where no deferred credit exists, the repayment should be charged immediately to income. Repayment of a grant related to an asset should be recorded by increasing the carrying amount of the asset or reducing the deferred income balance by the amount repayable. The cumulative additional depreciation that would have been charged to date in the absence of the grant should be charged immediately to income."

53. Essentially, the findings of this report support the above-mentioned recommendations; however, the conclusions could be re-emphasised, revised or expanded by the Group in the following or other ways:

(a) Although this paper has presented arguments supporting the contention that government grants could be credited directly to shareholders' funds, it is still felt that this would be an inappropriate treatment, and the previous recommended practice could be endorsed;

(b) The practices described above in Conclusions state that it is an acceptable alternate procedure to deduct the grant from the carrying amount of the asset concerned. However, for the reasons advanced within this paper, this position could be reconsidered. Consideration should be given to the distortionary impact of the netting method and the fact that the elementary distinction in financial accounting concerning the sources and application of funds is averted by this practice;

(c) The circumstances surrounding the repayment of a grant have been outlined above. If a charge is made to income it should be under the heading "Unusual item", if it qualifies as a material amount. However, the recommendation could be modified to specify that the correction should be made against the current year's profit and not as a prior year adjustment. The Group's pronouncement "Unusual charges and credits" further prescribes the treatment of such items. 7/

Notes

1/ Jones Martha, CA Magazine "The loan arrangers", June 1992, p. 43.

2/ Ibid., p. 44.

3/ Commission of the European Communities, Paper of the Accounting Advisory Forum, "Accounting for Government Grants", May 1992.

4/ Canadian Institute of Chartered Accountants, "Investment Tax Credits", July 1984.

5/ Hillier, Diana, CA Magazine "New Departures for transfers", January 1991, p. 40.

6/ Conclusions on Accounting and Reporting by Transnational Corporations (United Nations publication, Sales No. 88.II.A.18), paras. 171-172.

7/ Ibid., paras. 135-136.